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No. 93-

IN THE
Supreme Court of the United States
OCTOBER TERM, 1993

NCR CORPORATION,
Petitioner,
v.
TAXATION AND REVENUE DEPARTMENT
OF THE STATE OF NEW MEXICO,
Respondent.

Petition for a Writ of Certiorari to the Court of Appeals of New Mexico

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. Whether the prohibition of the Foreign Commerce Clause against state taxes that inevitably cause international multiple taxation precludes a state from taxing a corporation's foreign source dividends, interest, and royalties on which the corporation has already paid taxes on an unapportioned basis to foreign countries.

2. Whether the fair apportionment requirement of the Commerce and Due Process Clauses precludes a state from including in a corporation's apportionable tax base income received from its unitary subsidiaries without taking account of the subsidiaries' income-producing factors in the apportionment formula.

RULE 29.1 STATEMENT

Petitioner NCR Corporation is a wholly-owned subsidiary of American Telephone & Telegraph Company, which itself has no parent corporation. Petitioner's subsidiaries, other than wholly-owned subsidiaries, are as follows:

NCR Ghana Limited

NCR Japan, Ltd.

NCR (Nigeria) Limited

NCR (Thailand) Ltd.

TABLE OF CONTENTS

	Page
QUESTIONS PRESENTED	i
RULE 29.1 STATEMENT	ii
TABLE OF AUTHORITIES	v
OPINIONS BELOW	1
JURISDICTION	1
CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED	2
STATEMENT	2
1. NCR's Business	3
2. NCR's Dividend, Interest, and Royalty Income Received from Its Unitary Foreign Subsidiaries	4
3. New Mexico's Taxing Scheme	5
4. The Assessment	6
5. The Decisions Below	7
REASONS FOR GRANTING THE PETITION	9
I. THE STATE COURT'S DECISION CONDONING INTERNATIONAL MULTIPLE TAXATION THAT INEVITABLY RESULTS FROM NEW MEXICO'S TAXING SCHEME CANNOT BE RECONCILED WITH THIS COURT'S FOREIGN COMMERCE CLAUSE JURISPRUDENCE	10

TABLE OF CONTENTS—Continued

Page

II. THE STATE COURT'S RULING THAT INCOME FROM UNITARY SUBSIDIARIES MAY BE INCLUDED IN THE APPORTIONABLE TAX BASE WITHOUT INCLUDING THE SUBSIDIARIES' FACTORS IN THE APPORTIONMENT FORMULA DISPOSES OF THE ISSUE THAT THIS COURT LEFT OPEN IN *MOBIL* AND CREATES A CONFLICT AMONG STATE COURTS OF LAST RESORT.. 15

III. THE ISSUES OF BOTH INTERNATIONAL MULTIPLE TAXATION AND "FACTOR REPRESENTATION" RAISED BY THE DECISION BELOW ARE RECURRING QUESTIONS OF GREAT PRACTICAL IMPORTANCE 19

CONCLUSION 22

APPENDICES 1a

Appendix A:

Opinion of the Court of Appeals of New Mexico, May 6, 1993 ..... 1a

Appendix B:

Decision and Order of the Taxation and Revenue Department of New Mexico, March 18, 1991 ..... 19a

Appendix C:

Order Denying Petition for Writ of Certiorari by the Supreme Court of New Mexico, July 8, 1993.... 70a

Appendix D:

New Mexico Statutes Involved 71a

TABLE OF AUTHORITIES

Cases — Page

American Tel. & Tel. Co. v. Wisconsin Dep't of Revenue, 143 Wis. 2d 533, 422 N.W.2d 629 (Ct. App. 1988) 16, 17-18
Container Corp. of Am. v. Franchise Tax Bd., 463 U.S. 159 (1983) ..... *passim*
Hans Rees' Sons, Inc. v. North Carolina ex rel. Maxwell, 283 U.S. 123 (1931) 19
Homart Dev. Co. v. Norberg, 529 A.2d 115 (R.I. 1987) 16, 18-19
Japan Line, Ltd. v. County of Los Angeles, 441 U.S. 434 (1979) ..... *passim*
Kraft Gen. Foods, Inc. v. Iowa Dep't of Revenue and Finance, 112 S. Ct. 2365 (1992) 21
Mobil Oil Corp. v. Commissioner of Taxes, 445 U.S. 425 (1980) ..... *passim*
NCR Corp. v. Commissioner of Revenue, 438 N.W.2d 86 (Minn.), *cert. denied*, 493 U.S. 848 (1989) 16
NCR Corp. v. Comptroller of the Treasury, 313 Md. 118, 544 A.2d 764 (1988) 16, 19
NCR Corp. v. South Carolina Tax Comm'n, 304 S.C. 1, 402 S.E.2d 666 (1991) 16-17, 19
Tambrands, Inc. v. State Tax Assessor, 595 A.2d 1039 (Me. 1991) 16, 17
Underwood Typewriter Co. v. Chamberlain, 254 U.S. 113 (1920) 19

Constitution of the United States

U.S. Const., amend. XIV, § 1 2
U.S. Const., art. I, § 8, cl. 3 2

Statutes

I.R.C. §§ 61, 1504 20
I.R.C. §§ 861(a), 862(a) 14
I.R.C. §§ 871-872, 1441-1442 14
I.R.C. §§ 951-964 7
28 U.S.C. § 1257(a) 2
N.H. Rev. Stat. Ann. § 77-A:3, II(b) (1991) 20

TABLE OF AUTHORITIES—Continued

	Page
N.M. Stat. Ann. (Michie 1978) (1993 Repl.)	
§ 7-2A-2(C)	5
§ 7-2A-2(I)	5
§ 7-2A-3(A)	5
§ 7-2A-8.4	5
Ohio Rev. Code Ann. § 5733.04(I)(2) (Anderson 1991)	20
Utah Code Ann. § 59-7-303(4) (1992)	20
Va. Code Ann. §§ 58.1-302, 58.1-402(C)(8) (Michie 1991 & Supp. 1993)	20
Other Authorities	
Internal Revenue Service, *Statistics of Income Bulletin*, Vol. 12, No. 2 (Fall 1992)	21
Internal Revenue Service, Statistics of Income Division, *Compendium of Studies of International Income and Taxes*, Pub. 1267 (9-91)	21
1 Multistate Corporate Income Tax Guide (CCH) ¶¶ 79, 125 (1993)	20
American Law Inst., *Federal Income Tax Project*, International Aspects of United States Income Taxation 6-7 (1987)	13

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PETITION FOR A WRIT OF CERTIORARI

NCR Corporation respectfully petitions for a writ of certiorari to review the judgment of the Court of Appeals of New Mexico in this case.

OPINIONS BELOW

The opinion of the Court of Appeals of New Mexico (App. A at 1a-8a) is reported at — N.M. —, 856 P.2d 982. The opinion of the Taxation and Revenue Department of the State of New Mexico (App. B at 19a-69a) is unreported.

JURISDICTION

The judgment of the Court of Appeals of New Mexico was entered on May 6, 1993. The Supreme Court of the State of New Mexico denied NCR's petition for cer-

tiorari on July 8, 1993. App. C at 70a. The jurisdiction of this Court rests on 28 U.S.C. § 1257(a).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The Commerce Clause of the United States Constitution, U.S. Const., art. I, § 8, cl. 3, provides: "The Congress shall have Power . . . [t]o regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes."

The Due Process Clause of the Fourteenth Amendment of the United States Constitution, U.S. Const., amend. XIV, § 1, provides: "No State shall . . . deprive any person of life, liberty, or property, without due process of law."

Relevant portions of the New Mexico statutes are set forth at App. D at 71a-74a.

STATEMENT

This case raises two issues of great significance for state taxation of multistate and multinational corporations. Both issues arise out of the fact that New Mexico, like most other states, includes in a corporation's apportionable tax base income the corporation receives from its unitary foreign subsidiaries, but does not include the foreign subsidiaries' income-producing factors in the formula used to apportion such income. When, as in this case, the income is received in the form of dividends, interest, and royalties from foreign subsidiaries, and the recipient has already been taxed on that income by foreign countries on an unapportioned basis, the state's failure to provide for "factor representation" of the subsidiaries' factors in the parent's apportionment formula inexorably leads to international multiple taxation. The result is difficult to square with this Court's Foreign Commerce Clause jurisprudence barring state taxes that "inevitably"

cause international multiple taxation. *Japan Line, Ltd. v. County of Los Angeles,* 441 U.S. 434, 447 (1979).

The state's failure to provide for "factor representation" also raises a critical issue under the Court's "domestic" Commerce and Due Process Clause jurisprudence. In *Mobil Oil Corp. v. Commissioner of Taxes,* 445 U.S. 425 (1980), the Court explicitly left open the question whether the inclusion of dividend income from unitary subsidiaries in the parent's apportionable tax base requires that the subsidiaries' factors be reflected in the parent's apportionment formula. *Id.* at 441 n.15. Justice Stevens, who did address this question, observed that unless the subsidiaries' factors were reflected in the taxpayer-parent's apportionment formula, "the inclusion of earnings attributable to those corporations . . . will inevitably cause [the taxpayer-parent's] . . . income to be overstated." *Id.* at 461 (Stevens, J., dissenting) (footnote omitted). This case provides the Court with an opportunity to resolve this issue, which has spawned division and confusion in the state courts.

1. NCR's Business

The facts, which have been stipulated, are not in dispute. Petitioner NCR Corporation is a Maryland corporation with its corporate headquarters and principal place of business in Dayton, Ohio. NCR is engaged in the manufacture and sale of business equipment and machines, including cash registers, automated bank tellers, and computers. During the years at issue (1981-87), NCR conducted business directly in all 50 states and in many foreign countries. In New Mexico, NCR transacted business through the sale of its products and related supplies and services.

In addition to the business that NCR conducted directly within the United States and abroad, NCR conducted business indirectly through domestic and foreign subsidiaries. From an operational perspective, NCR's business was carried on in the same manner, whether

conducted directly by NCR through branches and divisions or indirectly through subsidiaries and whether conducted domestically or internationally. Indeed, it has been stipulated that "[t]he business conducted by NCR Corporation throughout the world, both directly and through its domestic and foreign subsidiaries, is a single, integrated unitary business." Stipulation of Facts ¶ 8 (App. B at 22a-23a).[1]

2. NCR's Dividend, Interest, and Royalty Income Received from Its Unitary Foreign Subsidiaries

NCR had approximately 75 foreign subsidiaries which conducted business in some 150 foreign countries. All but a few of these subsidiaries were wholly owned by NCR. None of them conducted business in New Mexico. From the unitary business carried on with its foreign subsidiaries, NCR derived substantial income in the form of dividends, interest, and royalties. For the years in question, the amounts were as follows:

Year	Dividends	Interest	Royalties
1981	$ 34,416,543	$21,730,821	$ 40,590,222
1982	35,214,185	28,320,913	47,897,917
1983	45,963,133	19,445,024	54,464,120
1984	50,167,524	16,157,574	73,833,474
1985	63,994,155	7,836,796	86,296,270
1986	73,289,419	11,765,099	100,039,780
1987	246,229,126	5,458,622	149,774,394

Stip. ¶ 29 (App. B at 29a-30a).

During the years at issue, NCR paid more than $94 million in income taxes that foreign countries imposed upon NCR on the dividends, interest, and royalties NCR received from its unitary foreign subsidiaries. Stip. ¶ 30

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[1] The Decision and Order of the New Mexico Taxation and Revenue Department adopted the Stipulation of Facts verbatim in its Findings of Fact. App. B at 20a-38a. All references to the Stipulation of Facts are hereinafter denominated "Stip." followed by a paragraph reference.

(App. B at 31a-33a).[2] At the same time, these dividends, interest, and royalties constituted on average more than 62 percent of the income that NCR included in its apportionable New Mexico tax base. Compare Stip. ¶ 29 (App. B at 29a-30a) with Stip. ¶ 33 (App. B at 34a-35a). During the years at issue, New Mexico taxed an apportioned share of these dividends, interest, and royalties. Stip. ¶ 36 (App. B at 36a).

3. New Mexico's Taxing Scheme

New Mexico imposes its corporate income tax upon the "net income" of every domestic corporation and of every foreign corporation doing business in the state. N.M. Stat. Ann. § 7-2A-3(A) (Michie 1978) (1993 Repl.). "Net income" is defined as federal taxable income, as adjusted for New Mexico tax purposes. *Id.* §§ 7-2A-2(C), 7-2A-2(I).[3] For the years at issue, NCR filed returns and paid taxes to New Mexico on a federal consolidated basis in conformity with New Mexico law. *Id.* § 7-2A-8.4; Stip. ¶ 5 (App. B at 21a). Under this filing method, NCR and its domestic subsidiaries—hereinafter collectively and interchangeably referred to as "NCR"—were in substance treated as a single taxpayer.[4] Thus, transactions between members of the domestic consolidated group, such as payments of dividends, interest, and royalties, were effectively eliminated; the domestic group's apportionable income was determined on the basis of its

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[2] These taxes are in addition to the taxes that NCR's foreign subsidiaries paid to foreign countries on their own income. See Stip. ¶¶ 15, 30 (App. B at 25a-26a, 31a-33a). NCR's taxes were typically withheld by NCR's foreign subsidiaries, which paid the taxes to the foreign country on behalf of NCR. Stip. ¶ 15 (App. B at 25a-26a).

[3] None of these adjustments is at issue here.

[4] The tribunals below drew no distinction between NCR and its domestic consolidated group, and no issue in this case turns on that distinction.

transactions with third parties; and the domestic group's combined factors were employed to apportion its income to New Mexico.

Foreign corporations are not included in a federal consolidated return. Consequently, although NCR's relationship to its unitary domestic and foreign subsidiaries was virtually identical, Stip. ¶¶ 7, 8 (App. B at 22a-23a), the foreign subsidiaries were treated quite differently from the domestic subsidiaries for New Mexico income tax purposes. Specifically, there was no consolidation of the foreign subsidiaries' and NCR's operating income from their collective dealings with third parties; the foreign subsidiaries' dividend, interest, and royalty payments to NCR were included in—rather than eliminated from—NCR's apportionable tax base; and, most importantly, the foreign subsidiaries' income-producing factors were not reflected in NCR's apportionment formula.

4. The Assessment

In filing its New Mexico tax returns, NCR excluded from taxable "net income" the dividends, interest, and royalties it received from its foreign subsidiaries. NCR's return position rested on the theory that New Mexico could not include the dividends, interest, and royalties in NCR's apportionable tax base under the Foreign Commerce Clause because such income was subject to tax on an unapportioned basis by foreign countries. New Mexico's taxation of even an apportioned share of such income, NCR maintained, would inevitably lead—and had in fact led—to international multiple taxation in violation of *Japan Line*. In the course of administrative proceedings, NCR took the alternative position that, if the disputed income was apportionable by New Mexico, then, under both the Commerce and Due Process Clauses, the income-producing factors of its foreign subsidiaries should be reflected in the formula employed to apportion the consolidated group's income. The New Mexico Taxa-

tion and Revenue Department (the "Department") rejected these views and assessed NCR for taxes which are currently calculated as $267,036. Stip. ¶ 36 (App. B at 36a).[5]

5. The Decisions Below

NCR timely protested the assessments and renewed its Commerce and Due Process arguments in a formal hearing before the Department. Stip. ¶ 26 (App. B at 27a-28a). The Department recognized that "[i]f *Japan Line* were the Supreme Court's last word on the application of the Foreign Commerce Clause to states' efforts to impose their apportioned income taxes to foreign source income, there would be no need for further analysis . . . ." App. B at 46. Accordingly, "NCR would prevail upon its claim, based upon the fact that it is subject to income taxation on the foreign source income by its foreign host countries as well as in the state of New Mexico, constituting prohibited multiple taxation." *Id.*

The Department nevertheless found *Japan Line* distinguishable from the instant case on the same grounds that this Court had distinguished *Japan Line* in *Container Corp. of Am. v. Franchise Tax Bd.*, 463 U.S. 159 (1983). In *Container*, this Court sustained California's worldwide unitary combined reporting method as applied to a United States multinational corporation over the objection, *inter alia*, that it resulted in multiple international taxation in violation of the strictures of the Foreign Commerce Clause articulated in *Japan Line*. In addressing this claim, the Court in *Container* had observed that "the double taxation in this case, although real, is not the 'inevitabl[e]' result of the California taxing

[5] NCR also raised additional constitutional claims directed specifically to New Mexico's taxation of hypothetical dividend income that NCR was deemed to have received from its controlled foreign corporations under Subpart F of the Internal Revenue Code. I.R.C. §§ 951-964. NCR is not pressing its separate claim with respect to such income in this Court.

scheme." *Container*, 463 U.S. at 188 (quoting *Japan Line*, 441 U.S. at 447). While expressing the view that this Court "in *Container* did not clearly explain the concept of 'inevitability,'" App. B at 49a, the Department nonetheless concluded that there was no "inevitable" multiple taxation in this case because not every foreign country in which NCR earned dividends, interest, and royalties exercised its right to tax such income on an unapportioned basis. *Id.* at 49a-50a.

The Department also rejected NCR's alternative argument that if the income derived from its unitary foreign subsidiaries were included in its apportionable tax base, NCR would be entitled to have the subsidiaries' income-producing factors reflected in its apportionment formula. Noting that this Court had left this issue open in *Mobil*, App. B at 54a, and that NCR's argument was "[a]t first blush, . . . compelling," App. B at 55a, the Department rejected the claim on the ground that NCR had not proved sufficient distortion in New Mexico's apportionment from the failure to include the subsidiaries' factors in NCR's apportionment formula.

The New Mexico Court of Appeals affirmed. App. A at 18a. Like the Department, the Court of Appeals found *Japan Line* inapposite on the theory that "the basic premise and holding of the Court in *Container Corp.* is controlling here." App. A at 9a. The New Mexico court reasoned that this Court's refusal to strike down California's apportioned tax in *Container* justified its own refusal to strike down New Mexico's apportioned tax in the instant case. The court below did not address the differences between the state taxes imposed in *Container* and those imposed in this case. Specifically, it did not consider that California's taxing scheme in *Container* included both the unitary group's operating income in the apportionable tax base as well as the foreign subsidiaries' income-producing factors in the apportionment formula. Instead, the court embraced the view that this case, like *Container*, simply involved application of the principle

that a state need not "give up one method of allocation that may at times result in double taxation in favor of another allocation method that may also result in double taxation." App. A at 7a. Without further explanation, the court observed that in this case, "[u]nlike the situation in *Japan Line*, multiple taxation, although *real*, is not inevitable." *Id.* at 11a (emphasis supplied). The court found *Japan Line* was also distinguishable on the grounds that it involved a property tax rather than an income tax and that the taxpayer there was a foreign rather than a domestic entity. *Id.* at 6a, 8a.

With regard to NCR's alternative argument that it was entitled to have the subsidiaries' factors reflected in its apportionment formula if their dividends, interest, and royalties were included in its apportionable tax base, the court acknowledged that Justice Stevens had advanced this position in his dissent in *Mobil*. App. A at 16a. Although this Court explicitly reserved the question raised by Justice Stevens, *Mobil*, 445 U.S. at 441 n.15; *see also Container*, 463 U.S. at 168 n.5, the court below astonishingly declared that it was "guided by the rationale of the majority decision which *rejected* the views set forth in the dissent" (App. A at 16a) (emphasis supplied). In any event, the court concluded that NCR's contention should be rejected because NCR had failed to demonstrate that the exclusion of the subsidiaries' factors from the apportionment formula had led to a "grossly distorted result." *Id.* at 17a.

REASONS FOR GRANTING THE PETITION

The judgment of the New Mexico Court of Appeals warrants review by this Court for three compelling reasons. First, the court's decision condoning international multiple taxation is incompatible with this Court's Foreign Commerce Clause jurisprudence and, if left undisturbed, would undermine essential restraints on state tax power. At the very least, this Court's guidance is needed to clarify the distinction between taxes that are constitu-

tionally intolerable under *Japan Line* and those that can survive constitutional scrutiny under *Container*. Second, the state court's denial of NCR's right to inclusion of its unitary subsidiaries' factors in its apportionment formula, despite the inclusion in NCR's apportionable tax base of income received from those subsidiaries, disposed of a critical issue that this Court explicitly left open in *Mobil* and that has created a conflict among state courts of last resort. This Court should address that issue and resolve that conflict. Third, the issues of both international multiple taxation and "factor representation" present recurring questions of profound practical importance that merit plenary consideration in their own right.

I. THE STATE COURT'S DECISION CONDONING INTERNATIONAL MULTIPLE TAXATION THAT INEVITABLY RESULTS FROM NEW MEXICO'S TAXING SCHEME CANNOT BE RECONCILED WITH THIS COURT'S FOREIGN COMMERCE CLAUSE JURISPRUDENCE

In *Japan Line*, this Court held that the Foreign Commerce Clause barred a state from imposing a fairly apportioned personal property tax on cargo containers that had been taxed on an unapportioned basis abroad. Although the tax would have passed muster under the Court's Interstate Commerce Clause doctrine, 441 U.S. at 445-46, the Court held that the tax violated the more exacting demands of the Foreign Commerce Clause. Under the Foreign Commerce Clause, "a court must also inquire, first, whether the tax, notwithstanding apportionment, creates a substantial risk of international multiple taxation." *Id.* at 451. In addition, a court must determine "whether the tax prevents the Federal Government from 'speaking with one voice when regulating commercial relations with foreign governments.'" *Id.* The Court observed that "[i]f a state tax contravenes *either* of these precepts, it is unconstitutional under the Commerce Clause." *Id.* (emphasis supplied).

As the New Mexico Taxation and Revenue Department conceded—and the Court of Appeals did not disagree—NCR's claim is unassailable if *Japan Line* controls this case: "NCR would prevail . . . based upon the fact that it is subject to income taxation on the foreign source income by its foreign host countries as well as in the state of New Mexico, constituting prohibited multiple taxation." App. B at 46a. Just as Los Angeles County in *Japan Line* sought to subject the taxpayer to an apportioned tax on property that a foreign country had taxed on an unapportioned basis, so, too, in this case New Mexico seeks to subject NCR to an apportioned tax on income that foreign countries have already taxed on an unapportioned basis. Stip. ¶¶ 29-30, 36 (App. B at 29a-33a, 36a).

In an effort to deflect the force of this analogy, the state court relied on *Container*, which concerned California's apportioned income tax on the combined income of a multinational group of corporations. The taxpayer challenged the tax on the ground that, when considered in conjunction with taxes imposed on such income by foreign countries, California's levy subjected the income to international multiple taxation in violation of the Foreign Commerce Clause. In sustaining the tax, this Court found that the international multiple taxation it had condemned in *Japan Line* was constitutionally tolerable in *Container* principally because the double taxation in *Container*, "although real, is not the 'inevitabl[e]' result of the California taxing scheme.'" *Container*, 463 U.S. at 188 (quoting *Japan Line*, 441 U.S. at 447).[6]

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[6] The Court also distinguished *Japan Line* on the ground that the case involved a property tax rather than an income tax and that the taxpayer was foreign rather than domestic. *Id.* at 187-89. But these factors were largely subsumed within the Court's analysis of whether the international multiple taxation in *Container* was "inevitable" and hence intolerable.

The state court's reliance on *Container* is misplaced. The multiple taxation in *Container* was not "inevitable" because it resulted from two different methods of dividing the tax base: California employed formulary apportionment as a means of dividing the tax base, whereas other countries used separate accounting as a means of dividing the tax base. "Whether the combination of the two methods results in the same income being taxed twice or in some portion of income not being taxed at all is dependent solely on the facts of the individual case." *Id.*

In *Japan Line* and the instant case, by contrast, there was no effort by the foreign taxing jurisdictions to divide the tax base. Rather they allocated 100 percent of the tax base to themselves. Consequently, when Los Angeles County or New Mexico sought to impose an apportioned tax on the same tax base, multiple taxation was "inevitable." Because foreign countries subjected 100 percent of the relevant base to tax, *any* apportioned tax imposed by another jurisdiction would result in multiple taxation. In short, we are not dealing here, as we were in *Container*, with two different methods of "divid[ing] the pie." *Id.* Rather, here (as in *Japan Line*) the entire pie has been subjected to tax by the foreign jurisdiction which leaves the states no room to tax even an apportioned slice.

There is a further point of distinction between *Container* and the instant case that accounts for the inevitability of the multiple taxation here. In *Container*, the combined income *and the combined factors* of Container and its unitary foreign subsidiaries were considered in determining the income that was properly attributable to California. Hence there was no certainty that, by including the foreign subsidiaries' income in the apportionable tax base, California would in fact *tax* such income. Rather, as a result of the inclusion of the foreign subsidiaries' factors in the apportionment formula, the income appor-

tioned to California could decrease, increase, or remain the same.[7]

Here, by contrast, while the income that NCR derived from its unitary foreign subsidiaries was included in its New Mexico apportionable tax base, the factors of those subsidiaries were ignored in apportioning the income to New Mexico. Consequently, there was dead certainty that New Mexico would *tax*—not merely apportion—every dollar of dividends, interest, and royalties that NCR received from its foreign subsidiaries,[8] and, accordingly, dead certainty that there would be international multiple taxation when such income was taxed on an unapportioned basis by foreign countries.

There is no merit to the suggestion advanced by the Department below that the "inevitability" of the multiple international taxation occasioned by New Mexico's tax may be questioned because some foreign countries did not exercise their right to tax NCR's dividends, interest, and royalties. There is worldwide recognition of the principle that the nation where income originates (the source nation) has the primary right to tax income having its source within that nation.[9] The dividends, interest, and royalties paid to NCR by its foreign subsidiaries

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[7] When a state considers both the income and the factors of foreign subsidiaries in the apportionment, two things happen: first, the apportionable tax base *increases*, because of the inclusion of the foreign subsidiaries' income; second, the apportionment percentage *decreases*, because the foreign subsidiaries' property, payroll, and sales add to the denominators, but not the numerators, of the corporation's apportionment factors for the taxing state. Thus, depending on the relative impact of these two changes, the income apportioned to the state will decrease, increase, or remain the same.

[8] When income is added to the apportionable tax base without modifying the factors employed to apportion such income, the necessary result is to tax such income. *See* note 7 *supra*.

[9] American Law Inst., *Federal Income Tax Project, International Aspects of United States Income Taxation* 6-7 (1987).

have their source in foreign nations.[10] Consequently, in accordance with the "custom of nations" (*Japan Line*, 441 U.S. at 447, 454), most of the foreign source dividends, interest, and royalties paid to NCR by its unitary foreign subsidiaries have been taxed to NCR abroad. Stip. ¶ 30 (App. B at 31a-33a).[11] The fact that some countries may have chosen to forbear from exercising their primary right to tax such income does not transform the inexorable clash between New Mexico's taxing scheme and the scheme embraced by the international community into the adventitious overlap that the Court found constitutionally tolerable in *Container*. Nor, of course, can it justify the "inevitable" multiple taxation that results when foreign nations do indeed exercise this primary right. In any event, if the notion of the "inevitability" of international multiple taxation is to be tied to its universality, it is incumbent upon this Court to delineate such a dramatic retrenchment in its Foreign Commerce Clause doctrine.

Finally, insofar as there are differences between this case, *Japan Line*, and *Container*, they underscore the need for the Court's consideration of this controversy. *Japan Line* articulated the principles limiting state taxation of foreign commerce, but, in contrast to this case, in the context of a property tax rather than an income tax. *Container* applied those principles to an income tax, but, in contrast to this case, in the context of a worldwide combined tax base where the subsidiaries' factors were fully represented. This case provides the Court with an opportunity to apply *Japan Line*'s principles to a tax on income which has been taxed by foreign countries

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[10] *See, e.g.*, I.R.C. §§ 861(a), 862(a) (source of dividends and interest generally based on residence of payor; source of royalties generally based on where royalty-producing property is used).

[11] Consistent with this custom of nations, the United States generally imposes a tax on dividends, interest, and royalties paid by United States residents to nonresidents. I.R.C. §§ 871-872, 1441-1442.

but with respect to which "factor representation" has been denied. The Court's review is necessary to delineate these principles in a manner that displays greater sensitivity to Foreign Commerce Clause concerns than did the court below and to provide guidance for tribunals like the Department below, which found that *"Container* did not clearly explain the concept of 'inevitability.'" App. B at 49a.

II. THE STATE COURT'S RULING THAT INCOME FROM UNITARY SUBSIDIARIES MAY BE INCLUDED IN THE APPORTIONABLE TAX BASE WITHOUT INCLUDING THE SUBSIDIARIES' FACTORS IN THE APPORTIONMENT FORMULA DISPOSES OF THE ISSUE THAT THIS COURT LEFT OPEN IN *MOBIL* AND CREATES A CONFLICT AMONG STATE COURTS OF LAST RESORT

In *Mobil,* this Court held that a state could include within the apportionable tax base of a nondomiciliary corporation the dividends that it received from its subsidiaries so long as the taxpayer and its subsidiaries were engaged in a unitary business. Although the taxpayer in *Mobil* had resisted that conclusion, it claimed that if its dividend income was constitutionally apportionable on the theory that it was engaged in a unitary business with its subsidiaries, then its income should have been apportioned under a method that included the subsidiaries' factors in the apportionment formula.

The Court declined to reach this question because it was not timely raised. *Mobil,* 445 U.S. at 441 n.15; *see also id.* at 449. Justice Stevens, however, did address the question in his dissent, where he declared:

> Unless the sales, payroll, and property values connected with the production of income by the payor corporations are added to the denominator of the apportionment formula, the inclusion of earnings attributable to those corporations in the apportionable tax base will inevitably cause [the payee's in-state] income to be overstated.

Id. at 461 (Stevens, J., dissenting). The Court has subsequently expressed similar sentiments by observing that the fair apportionment requirement demands that "the factor or factors used in the apportionment formula must actually reflect a reasonable sense of how income is generated." *Container*, 463 U.S. at 169. *See also id.* at 168 n.5 (recognizing Justice Stevens' views in *Mobil*).

In holding that New Mexico could include NCR's dividends, interest, and royalties received from its unitary foreign subsidiaries in NCR's apportionable tax base while denying NCR the right to include the subsidiaries' factors in its apportionment formula, the court below has disposed of the issue this Court left open in *Mobil* and, in so doing, has created an irreconcilable conflict with decisions of other state courts. The Supreme Court of Maine and the Wisconsin Court of Appeals have each recognized a taxpayer's right to "factor representation" when income received from subsidiaries is included in the taxpayer's apportionable tax base. *Tambrands, Inc. v. State Tax Assessor*, 595 A.2d 1039 (Me. 1991); *American Tel. & Tel. Co. v. Wisconsin Dep't of Revenue*, 143 Wis. 2d 533, 422 N.W.2d 629 (Ct. App. 1988). The Supreme Court of Rhode Island has recognized a similar principle with respect to partnership income received by a corporation. *Homart Dev. Co. v. Norberg*, 529 A.2d 115 (R.I. 1987). Other courts, however, have agreed with the New Mexico Court of Appeals that "factor representation" is not constitutionally required, at least in the absence of a demonstration by the taxpayer that failure to provide for "factor representation" produces a "grossly distorted result." *NCR Corp. v. Comptroller of the Treasury*, 313 Md. 118, 544 A.2d 764 (1988); *NCR Corp. v. Commissioner of Revenue*, 438 N.W.2d 86 (Minn.), *cert. denied*, 493 U.S. 848 (1989);[12] *cf. NCR Corp. v. South*

[12] When this Court denied certiorari in the Minnesota *NCR* case, the *Tambrands* case had not yet been decided and the petitioner had not brought the *Homart* case to the Court's attention. *See* Petition for Certiorari, *NCR v. Commissioner of Revenue.*

Carolina Tax Comm'n, 304 S.C. 1, 21-23, 402 S.E.2d 666, 673-74 (1991) (recognizing failure to provide "factor representation" was "not ideally fair," but conditioning relief on proof of a "gross disparity" of "constitutional proportions").

In *Tambrands*, the question was whether Maine could constitutionally include dividend income that the taxpayer received from its unitary foreign subsidiaries in the taxpayer's apportionable tax base without including the subsidiaries' factors in the taxpayer's apportionment formula. Relying on this Court's decision in *Container* (*see* 595 A.2d at 1044-45) and on Justice Stevens' dissent in *Mobil* (*see id.* at 1044 n.9), the Maine Supreme Court concluded that the "ineluctable result" of including the income derived from the taxpayer's unitary foreign subsidiaries in the apportionable tax base while excluding their factors from the formula "is that more of the business activity of the unitary business is attributed to Maine than is the actual case." *Id.* at 1044. The court concluded:

> Maine cannot, under the fairness principles of the due process clause requiring that the income it taxes be rationally related to values connected to the taxing state, include in Tambrands' "apportionable tax base income from its . . . affiliates operating abroad . . . [and] apportion such income by factors reflecting only [Tambrands' domestic] operations." W. Hellerstein, *Dividing the State Corporate Income Tax Base: Developments in the Supreme Court and Congress*, appearing in *The State Corporation Income Tax* 293 (C. McLure, Jr. ed. 1984).

Id. (brackets in original).

In *American Tel. & Tel.*, the question was whether Wisconsin could constitutionally include dividend and interest income that the taxpayer received from its unitary subsidiaries in the taxpayer's apportionable tax base without including either the subsidiaries' property or,

alternatively, the value of the taxpayer's investment in its subsidiaries, in the property factor of the taxpayer's apportionment formula. The Wisconsin Court of Appeals acknowledged that this Court had failed to address the merits of this issue in *Mobil* (*see* 143 Wis. 2d at 548, 422 N.W.2d at 635), but noted that commentators had recognized the force of the constitutional attack leveled at

> apportionment formulas which allegedly give insufficient weight to the sales, property and payroll of subsidiaries which make dividend, interest, royalty, and other payments to the parent corporation which are included by the taxing state as income subject to apportionment.

143 Wis. 2d at 549, 422 N.W.2d at 635. The court concluded that the inclusion in AT&T's apportionable tax base of dividends and interest it received from its unitary subsidiaries, without adjustment of the apportionment formula's property factor to reflect the subsidiaries' contribution to the production of that income, was constitutionally impermissible. "[T]he apportionment formula used by the department does not reflect a reasonable sense of how AT&T's income is generated and taxes value earned outside the borders of Wisconsin, contrary to . . . the due process and commerce clauses of the United States Constitution." 143 Wis. 2d at 551, 422 N.W.2d at 636.

In *Homart*, the question was whether Rhode Island could include a nondomiciliary corporation's partnership income in the corporation's apportionable tax base without reflecting the partnerships' factors in the corporation's apportionment formula. In holding that "factor representation" was required, the Rhode Island Supreme Court declared:

> The inclusion of this income in Homart's net-income calculation for apportionment purposes necessarily requires that the payroll, property, and receipt factors that gave rise to it be included in the appor-

> tionment equation also. Otherwise, the net income is subject to an apportionment ratio that reflects only Homart's in-state and everywhere business activity when, in fact, this income did not arise from Homart's corporate business activity but instead arose out of the partnerships' business activities that were not reflected in the apportionment ratio.

Homart, 529 A.2d at 121.

Indeed, even those courts that have concluded, along with the court below, that "factor representation" is unnecessary in the absence of proof of "gross distortion," have recognized the unfairness of including income from unitary subsidiaries in the apportionable tax base without adjusting the apportionment formula to reflect the subsidiaries' income-producing activities. *See NCR Corp. v. Comptroller of the Treasury*, 313 Md. at 151, 544 A.2d at 780-81; *NCR Corp. v. South Carolina Tax Comm'n*, 304 S.C. at 21-22, 402 S.E.2d at 673-74. These courts' reliance on the good-enough-for-government-work defense that a theoretically defective apportionment can be justified so long as the resulting distortion is not too great raises a question that itself is worthy of this Court's review. *See, e.g., Underwood Typewriter Co. v. Chamberlain*, 254 U.S. 113, 121 (1920) (apportionment formula may be struck down as "inherently arbitrary"); *Hans Rees' Sons, Inc. v. North Carolina ex rel. Maxwell*, 283 U.S. 123, 133 (1931) (apportionment formula may be struck down as "intrinsically arbitrary"). When this question is considered in conjunction with the conflict that the decision below has created with decisions of other state courts, the need for this Court's guidance is clear.

III. THE ISSUES OF BOTH INTERNATIONAL MULTIPLE TAXATION AND "FACTOR REPRESENTATION" RAISED BY THE DECISION BELOW ARE RECURRING QUESTIONS OF GREAT PRACTICAL IMPORTANCE

Wholly apart from the incompatibility of the state court's decision with this Court's Foreign Commerce

Clause precedents and apart from the conflict that the decision has created with other state courts of last resort, the decision below warrants this Court's review because it presents recurring questions of great practical importance.

The issue raised by this case arises in virtually every state with a corporate income tax. Like New Mexico, the overwhelming majority of states include dividends, interest, and royalties that a corporate taxpayer receives from unitary foreign subsidiaries in the taxpayer's apportionable tax base.[13] Like New Mexico, the overwhelming majority of states fail to provide for "factor representation" when such income is included in a taxpayer's apportionable tax base. Indeed, petitioner is aware of only two instances in which a state by statute provides for "factor representation" with respect to such income. N.H. Rev. Stat. Ann. § 77-A:3, II(b) (1991) ("factor representation" for dividends from unitary foreign affiliates); Utah Code Ann. § 59-7-303(4) (1992) (same). Consequently, the questions raised by the decision below—both with respect to international multiple taxation and with respect to "factor representation"—are constantly arising in almost every corporate income tax state for thousands of taxpayers. These questions have resulted in widespread disputes between taxpayers and state taxing

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[13] The vast majority of states use federal taxable income as the starting point for calculating state taxable income. 1 Multistate Corporate Income Tax Guide (CCH) ¶ 125 (1993). The federal tax base generally includes dividends, interest, and royalties received from foreign affiliates. I.R.C. §§ 61, 1504. Accordingly, unless explicitly excluded, such foreign source income is includable in the apportionable tax base in most states. Although some states provide a complete deduction for dividends from foreign affiliates, most provide only a partial deduction or none at all. 1 Multistate Corporate Income Tax Guide (CCH) ¶ 79 (1993) (and paragraphs cited therein). Moreover, only a handful of states exclude foreign source interest or royalties from the apportionable tax base. *See, e.g.*, Ohio Rev. Code Ann. § 5733.04(I)(2) (Anderson 1991); Va. Code Ann. §§ 58.1-302, 58.1-402(c)(8) (Michie 1991 & Supp. 1993).

authorities, as illustrated by the cases already cited in this petition and many others that are currently pending in state courts and administrative tribunals.

The amount of taxes at stake in these controversies is enormous. Thousands of taxpayers annually receive billions of dollars in foreign source dividends, interest, and royalties,[14] and much of this income is includable in their state apportionable tax bases.[15] Indeed, NCR's foreign source dividends, interest, and royalties constituted on average more than 62 percent of its New Mexico tax base (*see supra* p. 5), and in 1986 NCR's foreign source income constituted its entire apportionable tax base. *See* Stip. ¶¶ 29, 33. *See also Mobil*, 445 U.S. at 430 (involving "substantial amounts received as dividends from its subsidiaries and affiliates operating abroad"); *Kraft Gen. Foods, Inc. v. Iowa Dep't of Revenue and Finance*, 112 S. Ct. 2365 (1992) (involving over $10 million of dividends received from unitary foreign subsidiaries).

In view of the large number of taxpayers that are subject to taxing schemes like New Mexico's and the significant amounts of tax dollars involved, the practical importance of this controversy is self-evident.

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[14] In 1986 alone, approximately $5.6 billion of dividends and $3.8 billion of interest, rents, and royalties were paid to large U.S. corporations (*i.e.*, those with total assets of at least $500 million) by their 7500 largest controlled foreign corporations. Internal Revenue Service, Statistics of Income Division, *Compendium of Studies of International Income and Taxes*, Pub. 1267 (9-91), 223. In 1988, 744 of these largest U.S. corporations filed information returns reflecting their holdings in controlled foreign corporations. Internal Revenue Service, *Statistics of Income Bulletin*, Vol. 12, No. 2 (Fall 1992), 71. When one takes account of smaller corporations, the total number of corporations with foreign subsidiaries is obviously much larger.

[15] Although the foreign source income figures cited in note 14 *supra* include amounts paid by both unitary and nonunitary affiliates, plainly the amounts attributable to unitary subsidiaries are substantial.

CONCLUSION

The petition for certiorari should be granted.

Respectfully submitted,

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